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INTELLIGENCE BRIEF

DISCUSSION OF PROFITS REVIVED IN THE USSR

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DISCUSSION OF PROFITS REVIVED IN THE USSR

After a 2-year lull a second round of public discussion of the use of profits as a single, universal criterion of the performance of industrial enterprises was featured in the Soviet press during August and September of this year. Like the original proposal of Professor Ye. G. Liberman of Khar'kov in 1962, the new proposals seek to reduce the number of quotas on inputs that are now assigned directly to enterprises by the central planning authorities and to rely on the efforts of enterprises to maximize profits -- to which all managerial bonuses would be tied. Although placing greater stress on improved pricing than did Liberman, the authors of the new proposals do not go as far as Liberman in proposing more freedom for enterprises, and they fail to specify in as great detail as Liberman the institutional changes required to implement their proposals.

The new proposals, like the original Liberman proposal, fall far short of advocating market socialism under which enterprises, although publicly owned, would react autonomously to market forces. By failing to provide for the abolishment of central determination of output, assortment, and delivery schedules, the new proposals would leave intact most of the present machinery for central planning of production and distribution. Although some features of the new proposals, such as interest charges on capital, may be implemented ultimately, many of the main features have little chance for adoption throughout the economy. Some of the proposals -- such as use of profits as a single success criterion for all branches of industry and the relaxation of central controls over individual enterprises -- have been criticized repeatedly by responsible academic and governmental organizations. In industries producing consumer goods, however, the chances for adoption of some of the main features of the proposals appear bright. The post-Khrushchev regime has approved extension of the testing in the garment industry of the use of the profit criterion together with a system of decentralization that goes even further than that advocated by either the Liberman or the new proposals.

1. Background

Public discussion of the use of profits in some form as the main criterion of success for evaluating enterprises began with publication of the Liberman proposal in Pravda in September 1962. 1/ In his

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proposal, Liberman contended that by using the single criterion of "profitability" -- profits divided by total (fixed plus working) capital -- the state would need to set only output, assortment, and delivery goals to guide enterprises. Under his proposal, enterprises would be free to determine their own plans for labor productivity, wage fund, capital investment, and introduction of new technology. Liberman's main proposal regarding prices was that they should be set centrally so as to make the production of all desired goods profitable; he did not recommend either the use of prices that include capital charges (full cost prices) or the use of free market prices.

Publication of the proposal raised a storm of discussion in the Soviet press that did not subside until the Plenum of the Central Committee of the Communist Party held late in November 1962, at which time Khrushchev referred the proposal to the Academy of Sciences and the planning authorities for further consideration. 2/

Since 1962, discussion of profits and profitability has continued in isolated articles in the Soviet press, some of which have gone far beyond the Liberman proposal in advocating changes in planning and management. Among the specific changes proposed during this period have been the adoption of interest charges on fixed and working capital, the adoption of full cost prices based on the "prices of production" formula for price determination, the substitution of bidding by enterprises on contracts for their central assignment, and the turning over to state trade of the distribution of producer goods. One of the most radical of the proposals was advanced by A. M. Birman, professor of economics at the Moscow Institute of National Economy, in March 1963. 3/ Birman, in an article published in Ekonomicheskaya gazeta, advocated the abolishing of central planning of production and distribution of all but a dozen or so principal raw materials and end products. Plans for production of all other products would be determined by individual enterprises on the basis of orders received from wholesale trade establishments and from direct contracting between producers and industrial consumers. Supplies of materials and equipment would be obtained, not through central allocations, but through state trade channels and direct contracts with producers. Enterprises would be assigned targets only for value of output, and central control would be exercised through unspecified indirect financial controls and "effective" material incentives and sanctions.

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2. Tangible Results of the Discussion to Date

To date, the public discussion of profits and profitability has had only two tangible results. First, a new bonus system for managerial employees, which was worked out jointly by economists of the Academy of Sciences and the State Committee for Labor and Wages on the basis of the public discussion of the Liberman proposal, is now being tested in 80 to 85 industrial enterprises. Second, a system of decentralized control more similar to that proposed by Birman than to that proposed by Liberman is now being tested in two garment enterprises.

a. New Bonus System*

Testing of the new bonus system began on 1 April 1964 in 80 to 85 enterprises in the chemical, machine building, metallurgical, cement, and textile industries. The system provides for the elimination of large bonuses for plan overfulfillment, makes new arrangements for financing bonus funds, and increases the number of criteria by which an enterprise is evaluated. Although some of the provisions of the new system are aimed at correcting defects of the present system that were pointed out by Liberman, the main points of the Liberman proposal -- the reduction of detailed regulation of enterprises and the reliance on profitability as a single, universal criterion of success -- were explicitly rejected by the designers of the new system.

b. Experiment in the Garment Enterprises**

The other test, which officially began on 1 July 1964, provides for two garment enterprises -- "Bol'shevik" in Moscow and "Mayak" in Gor'kiy -- to maximize profits on the basis of orders received from retail stores participating in the experiment. The enterprises are freed from centrally determined regulation except for new investment and for a requirement that they make maximum use of existing capacity. Prices of products are negotiated between the producer and the retail stores on the basis of established price lists, and the enterprises are free to purchase materials wherever they are available in the quality and design desired. Although the experiment provides for far more decentralization than proposed by Liberman, in a recent newspaper interview he claimed it as a test of his own proposal. On 20 October 1964 the USSR Sovnarkhoz approved extension of the experiment to many more enterprises in the garment and footwear industries. 6/

* For a more complete discussion of the new bonus system, see source 4/.

** For a more complete discussion of the experiment, see source 5/.

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3. Main Features of the New Proposals

The new round of proposals was initiated by an article by Academician V. A. Trapeznikov, director of the Institute of Automation and Telemechanics of the Academy of Sciences, published in Pravda on 17 August. Trapeznikov, in his article, repeats Liberman's proposal that the number of inputs subject to centrally set quotas be reduced and that control of enterprise expenditures be exercised by paying bonuses to enterprises for maximizing profits. Unlike Liberman, however, Trapeznikov would not free expenditures on wages entirely from central regulation, and he does not propose that enterprises be permitted to determine their own plans for internal capital investment and the introduction of new technology. To encourage enterprises to economize on their use of capital, Trapeznikov substitutes interest charges on fixed and working capital for Liberman's formulation of "profitability."

In response to Trapeznikov's article, a series of six articles -- three by enterprise officials, one by a planning official, and two by academic economists (including Liberman) -- was published in Pravda between 17 August and 20 September. Unlike the responses to the original Liberman proposal, which ranged from carping on minor points to denunciation of its main features, the responses to the Trapeznikov proposal agreed for the most part with his main ideas and used them as points of departure for the authors' own proposals.

Some of the responding proposals go beyond Trapeznikov's proposal in calling for increased freedom for individual enterprises; none goes as far as the more extreme of the earlier proposals, like Birman's. Apparently taking a cue from the reaction to the original Liberman proposal, most of the proposals avoid spelling out the accompanying institutional changes and recommend retaining some central controls on enterprise wage funds. Only one, that by G. Kulagin, general director of the Leningrad Machine Tool Firm, specifically advocates that enterprises determine their own plans for internal investment and for the introduction of new technology. 7/

Other specific features of the new proposals include advocacy of full cost pricing -- not included in Liberman's proposal -- and the use of differential taxes to equalize profitability among enterprises in extractive industry. Although some of the proposals speak of supply and demand and the need for flexibility in the setting of prices, these statements refer to criteria for central determination of prices -- none

of the proposals advocates market determination of prices. One proposal, by I. Manvelov, director of the Moscow Kauchuk Chemical Plant, appears to advocate amalgamation of all enterprises now subordinate to the branch administrations of the regional sovnarkhozes into a series of giant firms and to turn the distribution of producer goods among them over to state trade and direct contracting. 8/ The new Liberman article, which is the last of the series, presents a defense of his earlier ideas and makes no new substantive proposals. 9/

4. Prospects

Extension of the experiment in the garment industry and the continued availability of the Soviet press for discussions of profits and profitability demonstrate a growing interest in the increased use of indirect financial controls in exercising central direction of individual enterprises. This interest is illustrated by an article welcoming the continuation of the discussion by S. A. Afanas'yev, chairman of the RSFSR Sovnarkhoz, which was published in Pravda during the series of new proposals. 10/ Chances for adoption of the main features of the proposals throughout industry, however, do not yet appear bright.

The attitude of most Soviet economists is typified by the consensus of the Academy of Sciences' Scientific Council on Economic Accountability and the Material Stimulation of Production -- the organization to which the Liberman proposal was referred after the November 1962 Plenum. According to economist L. Gatovskiy, chairman of the council, the consensus of the council was that, although profit is an important criterion for evaluating individual enterprises, other criteria such as increased production, increased labor productivity, and successful introduction of new technology are of equal or greater importance in many industries. 11/

More recently, the Academy of Sciences' Scientific Council on the Improvement of Methods and Indicators of National Economic Planning, which is chaired by A. Korobov, a deputy director of Gosplan, spoke on some of the other main features of the proposals. At a meeting in the offices of Gosplan on 19 May 1964, the council, after reaffirming its condemnation of the use of profits as the single, universal criterion and of the entrusting to enterprises of the planning of targets such as the number of workers and cost of production, recommended that the proposals for adopting capital charges and for entrusting the distribution of producer goods to state trade be subjected to further discussion and to testing. 12/

Some of the features of the proposals -- such as the capital charge, which already has been adopted in Hungary and experimentally in East Germany -- may be adopted ultimately throughout industry. Such piecemeal adoption of some of the features, however, is not likely to bring about much improvement in economic efficiency. Past experience with bonuses for cost reduction indicates that many difficulties are encountered when an attempt is made to supplement existing direct assignments of the central planners with new indirect financial controls. In such cases, when conflicts arise between the direct assignments and the indirect controls, performance on direct assignments takes precedence in evaluating the enterprise. Thus piecemeal adoption of individual features of the latest proposals may increase the number of headaches of enterprise directors without increasing their freedom of action.

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1. Pravda, 9 Sep 62. U.
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3. Ekonomicheskaya gazeta, 30 Mar 63, p. 7. U.
4. CIA. CIA/RR CB 64-43, Aftermath of the Liberman Proposal: the USSR Tests a New Bonus System for Industrial Managers, Jun 64. C.
5. CIA. CIA/RR CB 64-56, Soviet Light Industry Plants Test Consumer Sovereignty, Sep 64. C.
6. New York Times, 21 Oct 64, p. 1. U.
7. Pravda, 15 Sep 64. U.
8. Ibid., 19 Sep 64. U.
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11. Voprosy ekonomiki, no 11-63, p. 134. U.
12. Ibid., no 7-64, p. 154. U.

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